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SUBJECT: MEXICAN CENTRAL BANK REGIONAL DELEGATE PAINTS A GRIM PICTURE OF THE ECONOMY

REF: A) MEXICO 3345 B) MONTERREY 495

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¶1. (SBU) Summary. On November 14 the Nuevo Leon regional delegate of the Mexican Central Bank briefed the local American Chamber of Commerce on the U.S. financial crisis and its impact on Mexico. His analysis reflects many negative trends and portrays a much more negative picture of the Mexican economy than described by the Mexican Treasury Ministry. In particular, delegate Agustin del Rio emphasized that the Central Bank's immediate priority will have to be market intervention in order to maintain a stable exchange rate. He foresaw long term threats to the Mexican peso in view of dropping oil production, exports and remittances. He stated that the outlook for the Mexican economic growth has dimmed due to declines in the Mexican stock market, falling consumer demand and retail sales. Employment is not growing, wage growth is stagnant, and total bank credit is declining. End Summary.

Central Bank Interventions to Stabilize the Mexican Peso

¶2. (SBU) According to del Rio, the Mexican peso has lost value due to the 'flight to quality' to the U.S. dollar, and money is draining out of Mexico. Del Rio presented graphs showing that the Mexican peso devalued 16% from September 11 to October 13, the Mexican stock market fell 19%, and Mexico country risk, measured by EMBI+ (Emerging Markets Bond Index plus) rose from 200 basis points in September to 400 basis points. In addition, over \$6 billion dollars have been withdrawn from emerging markets (not just Mexico) in the last month or six weeks. Del Rio thought that the economy had not yet reached the bottom, and mutual funds would continue to pull investments from the emerging markets. He also worried that although the Federal Reserve and other Central Banks have invested in the commercial banks, there is still a lack of access to credit and liquidity.

¶3. (SBU) Del Rio stated that the Mexican Central bank will continue to intervene to stabilize the value of the peso (see reftel B). In addition, the U.S. Federal Reserve has offered \$30 billion dollars to the Central Bank to support the Mexican currency. That said, Del Rio is still worried about the long term exchange rate, since Mexico's oil production and exports are declining, as are worker remittances, all three of which will bring fewer dollars into the Mexican economy.

Impacts on the Real Mexican Economy

¶4. (SBU) The Central Bank found that the U.S. financial crisis has resulted in sharp reductions in the growth of consumer spending, retail sales, exports and industrial production. Mexican industrial output is closely tied to the U.S. index of manufacturing production, and the U.S. index is falling rapidly. Del Rio did not present Mexican figures, but he expected them to follow suit. Del Rio did present charts showing that growth in Mexican private consumption, bank consumption credit and retail sales have fallen since March 2008, although they are still positive. In addition, Mexican worker remittances are dropping following the fall in U.S. construction employment. The Central Bank statistics also show that since August there has been a large decline in the growth of gross capital formation and a small drop in investment growth. In general manufacturing exports are still increasing at 10% per year according to the most recent statistics, although automotive exports declined by 4%. The same trend holds for industrial production, manufacturing output, and electrical consumption, where annual growth rates have fallen substantially since December 2007, and each of the indexes are now growing at only 1-2% per year.

¶5. (SBU) The slowdown in the Mexican economy has also affected employment and wages. Since December 2007 the annual increase in total wages have fallen from 5.3% to 1.8%, formal employment growth has declined from 3.9% to 1.6%, and the mean wage in the formal economy, which was up 1.4% in December 2007, is now stagnant at 0.1% growth. The growth in formal employment has fallen from 3.87% in December 2007 to 1.64% in September ¶2008. The percentage increase in permanent formal employment

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fell from 4.3% in April 2007 to 1.5% in September 2008, while the increase in temporary workers has fallen from 14.4% in July 2006 to 3.2% in September 2008.

Mexican Central Bank Distributing Business Surveys

¶6. (U) Del Rio gave his presentation to the American Chamber of Commerce monthly board meeting, and requested that board members fill out a survey of their perceptions of business conditions. Del Rio had requested that the Consulate arrange for the briefing to the AmCham, so that he could gather more real time information on economic trends. Post will forward an electronic copy of the presentation (in English) upon request to the following e-mail address: heartneyep@state.gov

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¶7. (SBU) Comment. There is a clear division between the public stances of the Mexican Central Bank and the Ministry of Hacienda (Treasury). Hacienda argues that the U.S. financial crisis has had a much more mild impact on Mexico and that the Mexican economic fundamentals are solid. Del Rio acknowledged Hacienda's differing view, but countered that the numbers support the Central Bank position. End Comment.

WILLIAMSON